Supreme Court, U.S.
FILED
OCT 3 1986
JOSEPH F. SPANIOL, JR.
CLERK

NO. 86-561

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1986

GEORGE F. GRODE, INSURANCE COMMISSIONER OF THE COMMONWEALTH OF PENNSYLVANIA,

Petitioner

V.

UNITED SERVICES AUTOMOBILE ASSOCIATION, a Texas Reciprocal Interinsurance Exchange, USAA CASUALTY INSURANCE COMPANY, a Texas Stock Insurance Company, USAA LIFE INSURANCE COMPANY, a Texas Stock Insurance Company, USAA ANNUITY AND LIFE INSURANCE COMPANY a Texas Stock Insurance Company,

Respondents

Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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STATEMENT OF QUESTIONS PRESENTED FOR REVIEW

1. Whether rejection of abstention under the doctrine of Younger v. Harris, 401 U.S. 371 (1971), on the sole basis that a state administrative tribunal has no power to address constitutional claims conflicts with Ohio Civil Rights Commission v. Dayton Christian Schools, Inc., No. 85-488 (June 27, 1986), in light of the fact that, in Pennsylvania, a party to the state administrative proceeding may raise constitutional issues on appeal to a court.

2. Whether abstention under the doctrine of Railroad Commission v. Pullman, 312 U.S. 496 (1941), is inappropriate because, despite the existence of an unsettled question of state law which could pretermit the constitutional

questions, one of the challenges is a preemption claim and the plaintiff claims that its business reputation will be injured by an adverse state administrative ruling.

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IN THE SUPREME COURT OF THE
UNITED STATES
October Term, 1986
NO.

GEORGE F. GRODE, Insurance
of the Commonwealth of Pennsylvania,
Petitioner

v.

UNITED SERVICES AUTOMOBILE ASSOCIATION
A Texas Reciprocal Interinsurance
Exchange, USAA CASUALTY
INSURANCE COMPANY, a Texas stock
Insurance Company, USAA
LIFE INSURANCE COMPANY,
a Texas Stock Insurance Company,
USAA ANNUITY AND LIFE INSURANCE COMPANY,
a Texas Stock Insurance Company,
Respondents

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

The Attorney General of the Commonwealth of Pennsylvania, on behalf of petitioner, George F. Grode,[1] hereby petitions for a writ of certiorari

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[1]This action was filed against William J. Muir, III, Acting Insurance Commissioner in his official capacity. Mr. Grode succeeded Mr. Muir and he is substituted as petitioner pursuant to Rule 40.3 of the rules of this Court.

to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinion of the Court of Appeals (Pet. App. 39a-86a) is reported at 792 F.2d 356. The opinion and order of the District Court (Pet. App. 1a-38a.)are not reported.

STATEMENT OF JURISDICTION

The Court of Appeals filed its opinion on June 6, 1986. On August 22, 1986, a 30-day extension of time to file this petition for writ of certiorari was granted by the Court. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Section 641 of the Pennsylvania Insurance Act of 1921, as amended, Pa.Stat.Ann. tit. 40, § 281 (Purdon Supp. 1986), provides:

> Lending institutions, public utilities and holding companies not to be licensed
>
> (a) As used in this section:
>
> (1) "Lending Institution" means any institution that accepts deposits and lends money in the Commonwealth of Pennsylvania, including banks and savings and loan associations, but excluding insurance companies.
>
> * * * *
>
> (4) "Bank Holding Company" shall mean and include the definition of such term in section 2 of an act of Congress entitled the "Bank Holding Company Act of 1956," as amended:

provided, however, that if on or before the effective date of this act, a bank holding company has been granted an exeemption by the Board of Governors of the Federal Reserve System pursuant to section 4(d) of the Bank Holding Company Act of 1956, as amended, such bank holding company shall not be held to be a bank holding company within the meaning of section 2 of the Bank Holding Company Act of 1956, as amended.

(7) A "savings and loan holding company" shall mean and include the definition of such term as defined in Title 12, United States Code, section 1730(a)(1),(d), (e),(f), 12 U.S.C. 1430a.

* * * *

(b) No lending institution, public utility, bank holding company, savings and loan holding company or any subsidiary or affiliate of the foregoing, or officer or employe thereof, may, directly or indirectly, be licensed or admitted

as an insurer or be licensed to sell insurance in this State either as a broker or as an agent except that a lending institution or bank holding company, subsidiary or affiliate of a lending institution may be licensed to sell credit life, health and accident insurance and to sell and underwrite title insurance in accordance with regulations promulgated by the Insurance Commissioner.

(c) The Insurance Commissioner is authorized to promulgate regulations in order to effectuate the purposes of this section, which are to help maintain the separation between lending institutions and public utilities and the insurance business and to minimize the possibilities of unfair competitive practices by lending institutions and public utilities against insurance companies agents and brokers.

STATEMENT OF THE CASE

This is a civil rights action in which the respondents (plaintiffs below) challenged a provision of Pennsylvania's insurance laws as being violative of the Commerce, Due Process, Equal Protection, and Supremacy Clauses of the United States Constitution. On motions filed by petitioner (defendant below), the District Court dismissed the suit on abstention grounds. The Court of Appeals reversed.

1. United Services Automobile Association (USAA) is a reciprocal interinsurance exchange organization domiciled in San Antonio, Texas.[2] It

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[2]In a reciprocal interinsurance exchange,

(FOOTNOTE CONTINUED ON NEXT PAGE)

has been licensed by the Pennsylvania Department of Insurance (Department) to sell insurance in Pennsylvania since 1950.

In April of 1983, USAA Financial Services Company, a wholly owned subsidiary of USAA, applied for and received from the Federal Savings & Loan Insurance Corporation (FSLIC) permission

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(FOOTNOTE CONTINUED)

> individuals, partnerships, or corporations engaged in a similar line of business undertake to indemnify each other against a certain kind or kinds of losses by means of a mutual exchange of insurance contracts. . . whereby each member separately becomes both an insured and an insurer with several liability only.

2 Couch on Insurance, §18:11 at 614-15 (2d ed. 1984).

to organize and operate the "USAA Federal Savings Bank" (Bank) in San Antonio, Texas. The Bank also received permission from the FSLIC to serve as a unitary savings and loan holding company.[3] The Bank does not solicit deposits from Pennsylvania residents and does not do business in Pennsylvania.

The Pennsylvania Insurance Department Act of 1921 provides at Section 641:

> Lending institutions, public utilities and holding companies not to be licensed

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[3]Pennsylvania law, Pa. Stat. Ann. tit. 40, §281 (Purdon Supp. 1986), adopts the federal law definition of "savings and loan holding company" which provides: "any company which directly or indirectly controls an insured institution or controls any other company which is a savings and loan holding company by virtue of this subsection." 12 U.S.C. §1730 a(1)(D).

(a) As used in this section:

(1) "Lending institution" means any institution that accepts deposits and lends money in the Commonwealth of Pennsylvania, including banks and savings and loan associations, but excluding insurance companies.

* * * *

(b) No lending institution, public utility, bank holding company, savings and loan holding company or any subsidiary or affiliate of the foregoing, or officer or employe thereof, may, directly or indirectly, be licensed or admitted as an insurer or be licensed to sell insurance in this State either as a broker or as an agent except that a lending institution may be licensed to sell credit life, health and accident insurance and to sell and underwrite title insurance in accordance with regulations promulgated by the Insurance Commissioner.

(c) The Insurance Commissioner is authorized to promulgate regulations in order to effectuate the purposes of this section, which

> are to help maintain the separation between lending institutions and public utilities and the insurance business and to minimize the possibilities of unfair competitive practices by lending institutions and public utilities against insurance companies, agents and brokers.

Pa. Stat. Ann. tit. 40, §281 (Purdon Supp. 1986)(Act). The Department interprets Section 641 as requiring USAA to divest itself of ownership in the Bank.[4]

In attempting to convince the Department that it was not violating state law, USAA contended that Section 641 is ambiguous, and, if subsections (a)(1), (b) and (c) are read together,

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[4]The Department first questioned USSA's ownership of the Bank on July 3, 1986, and the legal staff of the Department formally communicated its position to USAA in writing on August 27, 1984. Court of Appeals Appendix (hereinafter "C.A. App.") at 39a-41a.

it becomes clear that sub-section (b) requires only that USAA, as an insurer, divest itself of ownership if the Bank does business in Pennsylvania. Because the Bank does business only in Texas, it was USSA's position that Section 641(b) did not apply and it need not divest itself of ownership of the Bank. See Pet. App. 12a.[5]

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[5]USAA's position was set forth in detail in an October 29, 1984 letter from USAA's counsel to the Department's chief counsel, a portion of which provides:

> We understand that the Department's concerns are based on an interpretation of Section 641 of the Insurance Department Act of 1921, as amended (40 Pa.C.S.A. §281) (hereafter "Section 641"), which holds that a foreign insurer transacting business in Pennsylvania may not be affiliated directly with a bank, even though the deposits, loans and operations of the bank have no nexus with the Commonwealth of Pennsylvania.

(FOOTNOTE CONTINUED ON NEXT PAGE)

2. Because the Department continued to maintain that USAA's ownership of the Bank violated Section 641, USAA, along with three of its subsidiary insurance companies, filed suit in the United States District Court for the Middle District of Pennsylvania on November 27, 1984, against the Acting Insurance Commissioner (Commissioner) seeking to enjoin the Department from revoking USAA's license to insure persons in Pennsylvania. Pet. App. 4a.

(FOOTNOTE CONTINUED)

> In our opinion, as discussed below, Section 641, properly interpreted, does not prohibit the indirect affiliation between USAA, a Texas-domiciled insurer, and a federal savings bank whose activities are strictly localized in San Antonio, Texas. Moreover, any interpretation of Section 641 that would prohibit USAA's affiliation with the Bank in this case would, on well-established standards, violate the United States Constitution.

C.A. App. at 45a-50a.

Alleging a cause of action under 42 U.S.C. § 1983, USAA contended that the Department's interpretation and application of Section 641 violated the Commerce, Supremacy, Due Process and Equal Protection Clauses of the United States Constitution. Pet. App. 20a, 50a.

On December 24, 1984, the Commissioner moved either to dismiss the complaint or stay the proceedings on abstention grounds. On that same date, the Department, through its legal staff, issued an "Order to Show Cause" directing USAA to appear at an administrative hearing to determine whether or not it was in violation of Section 641(b). USAA opposed the abstention motion, and in addition, on January 25, 1985, filed a

motion for summary judgment on preemption (Supremacy Clause) grounds.[6]

3. On September 30, 1985, the District Court dismissed the action on abstention grounds. Pet. App. 38a. In so doing, the court concluded that abstention was appropriate under each of the doctrines enunciated by this Court in Younger v. Harris, 401 U.S. 37 (1971); Railroad Commission of Texas v. Pullman, 312 U.S. 496 (1941); and Burford v. Sun Oil Co., 319 U.S. 315 (1943). Pet. App. 1a-38a.

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[6]USAA contended that Section 641(b), as applied to it, violated the Supremacy Clause because (1) Congress has occupied the entire field of regulating federal savings banks and (2) Section 641(b) was in actual conflict with federal law; namely the Home Owners' Loan Act of 1933, as amended, 12 U.S.C. § 1461 et seq., and the National Housing Act, as amended by the Savings and Loan Holding Company Amendments of 1967, 12 U.S.C. §§ 1730, 1730a.

The Court based its conclusion that Younger abstention was appropriate on three findings: (1) there was a "pre-existing state administrative proceeding," Pet. App. 33a; (2) Pennsylvania had a substantial interest in regulating the insurance industry, as recognized by Congress in the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1105, and therefore Pennsylvania's interest in going forward with its administrative proceeding was "sufficiently weighty" to justify abstention, Pet. App. 34a; and (3) USAA had an adequate forum to raise and vindicate its federal claims through Pennsylvania's state court system. Pet.App. 35a.[7]

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[7]Under Pennsylvania law, a proceeding to revoke or suspend an insurer's license is commenced with an order to show cause. The matter is assigned to a Department hearing officer

(FOOTNOTE CONTINUED ON NEXT PAGE)

(FOOTNOTE CONTINUED)

and the parties (i.e., the prosecutorial staff of the Department and the insurer) present their respective cases to the officer. The officer submits a recommended adjudication and order to the Commissioner who may either accept, reject or modify the officer's recommendation. This is precisely what has happened in this case. An order to show cause was issued in December of 1984; after various preliminary matters were resolved, two days of hearing were held before a hearing officer on November 14-15, 1985; post-hearing briefs were submitted in February and March of this year; and the parties are presently awaiting the Commissioner's determination.

If the determination is adverse to USAA, it may file an appeal as of right to the Pennsylvania Commonwealth Court, 42 Pa.Cons.Stat. § 763, Pet. App. 92a-93a, and an appeal by allowance from an adverse Commonwealth Court decision to the Pennsylvania Supreme Court, 42 Pa.Cons.Stat. § 724, Pet. App. 92a. In addition, pending its appeals, USAA may apply for a stay or supersedeas of any adverse determination by the Commissioner. See Rule 1781, Pennsylvania Rules of Appellate Procedure, Pet. App. 90a-92a.

The District Court held also that Pullman abstention was appropriate. In reaching this result, the Court concluded that the case was "one in which there is clearly an unsettled and potentially dispositive issue of state law." Pet. App.12a. It further held that resolution of the state law issue in favor of USAA (i.e., Section 641(b) does not apply to USAA because the Bank does not do business in Pennsylvania) would obviate the need to reach USAA's constitutional claims. Pet. App. 16a. Finally, the Court concluded that the state statute in question was part of a comprehensive insurance regulatory scheme implemented under the power granted by Congress to the states under the McCarran-Ferguson Act, and therefore considerations of comity dictated that interpretation of

the statute be left, in the first instance, to "the state administrative machinery and eventually, through appeals, to the state court system." Pet. App. 17a.[8]

The District Court concluded finally that Burford abstention was proper. Citing Colorado River Water Conservation District v. United States, 424 U.S. 800, 814 (1976), the court held that the case involved "difficult questions of state law bearing on policy

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[8]The District Court rejected USAA's claim that it would be prejudiced by any adverse determination by the Commissioner. It did so because of the appellate remedies (including supersedeas) available to USAA. Pet. App. 19a. The court also rejected USAA's contention that, because one of its several constitutional claims was based on the Supremacy Clause, Pullman abstention was inappropriate. Pet. App. 20a.

problems of substantial public impact whose importance transcends the result in the case then at bar." Pet. App. 23a.

The court found that the policies implemented by Section 641 are "essentially state policies developed to protect state citizens and implement state concerns." It further concluded that, if the state procedure is permitted to run its course up through the state Supreme Court, "the state itself will have an opportunity to interpret and mold its own policies in this area of significant state concern, while at the same time, the federal question will be preserved for ultimate review by the United States Supreme Court, if necessary." Pet. App. 27a.[9]

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[9] The court rejected USAA's contention that the "business of insurance," as governed by the McCarran-

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The District Court chose to dismiss (rather than stay) USAA's federal claims because the "state administrative and court systems provide an opportunity for USAA to raise all of its claims and because successful pursuit of those claims in the state system will afford USAA all of the relief it requested from" the federal court. Pet. App. 36a.

(FOOTNOTE CONTINUED)

Ferguson Act, was not at issue. As the court reasoned: "[E]ven if § 641 does not directly regulate an integral part of the policy relationship between the insurer and the insured, Union Labor Life Insurance Co. v. Pireno, 458 U.S. 119, 129 (1982), the policies behind § 641 and designed to be implemented by § 641 may have everything to do with the relationship between insurers and insured. Formulation and implementation of such policies are strictly the province of the state's legislative and administrative bodies." Pet. App. 28a.

4. Affirmance by the Court of Appeals of any of the District Court's three bases for abstention would have permitted Pennsylvania's state courts to interpret Section 641 in the first instance and thus possibly obviate the need to address USAA's federal constitutional claims. However, the Court of Appeals held that none of the abstention doctrines were applicable and therefore remanded the case to the District Court to dispose of USAA's claims. Pet. App. 37a.

The Court of Appeals agreed with the District Court's analysis of Younger in all respects with one exception. It held that, because the administrative agency (i.e., the Insurance Department) did not have the authority to address USAA's federal constitutional

claims, its administrative proceeding was not a part of the "state judicial process" for purposes of Younger abstention. Pet. App. 77a-78a. On this basis alone, the Court of Appeals rejected the applicability of Younger abstention.

The Court of Appeals agreed that the state law question involving the interpretation of Section 641 was "unsettled," but nevertheless rejected abstention under Pullman for two reasons. First, although the Commissioner agreed to expedite the state proceedings and further agreed to a stay of any administrative order in the event of a decision adverse to USAA until the appellate judicial proceedings were completed, the court concluded that the "threat" of a license revocation was of such magnitude

that abstention would be improper.[10] The court also concluded that USAA's Supremacy Clause claim did not pose a "substantial federal constitutional claim" as required for Pullman abstention. And, although the Supremacy Clause claim was only one of several constitutional claims raised by USAA, it was "easily separable" from USAA's other claims and thus dictated against abstention. Pet. App. 67a.[11]

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[10]Only two of the three panel members joined in this rationale. Judge Becker, noting that the harm to USAA was not especially significant, concluded that the majority's holding on this issue "may have dangerously broad implications" because it creates a "precedent that could allow virtually any litigant faced with relatively complex state litigation to avoid the application of the Pullman abstention doctrine." Pet. App. 79a.

[11]At the time of the filing of this petition, the District Court has pending before it USSA's motion for summary judgment based upon its Supremacy Clause claim.

Finally, the Court of Appeals reversed the District Court's finding that Burford abstention was proper. The court concluded that (1) Section 641 did not involve the "business of insurance" under McCarran-Ferguson, (2) no complicated regulatory scheme was at issue, (3) the interpretation of Section 641 did not require consideration of any other Pennsylvania statute, and (4) no local conditions or special expertise was required to interpret the statute. Pet. App. 68a-73a.

REASONS FOR GRANTING THE WRIT

1. The principles applied by the Court of Appeals in rejecting abstention under the Younger doctrine are in direct conflict with those endorsed by this Court in Ohio Civil Rights Commission, et al. v. Dayton Christian Schools, Inc., et al., No. 85-488 (June 27, 1986)

The Court of Appeals reversed the District Court's holding that Younger abstention was proper for one reason only - USAA could not raise constitutional claims during its administrative proceeding before the Insurance Department, and therefore that proceeding was not a part of the state's judicial process for Younger purposes. Pet. App. 77-78a. But, in Ohio Civil Rights Commission, et al. v. Dayton Christian Schools, Inc., et al., No. 85-488 (June 27, 1986), this Court expressly rejected the rationale employed by the Court of Appeals.

In Dayton, this Court specifically held that Younger abstention is appropriate so long as the "constitutional claims may be raised in state court judicial review of the administrative proceeding." Slip op. at 8-9. USAA did not, nor could it, argue that it has no right of appeal from an adverse determination to the Pennsylvania state courts and that those courts, on appeal, may not consider constitutional claims. Indeed, state law specifically obligates Pennsylvania's appellate courts to decide whether an agency's determination is "in violation of the constitutional rights of the appellant...." 2 Pa. Cons. Stat. § 704. See Pet. App. 89a-90a. "A party who proceeded before a Commonwealth agency under the terms of

a particular statute shall not be precluded from questioning the validity of the statute in the appeal. . . ." 2 Pa. Cons. Stat. §703(a), Pet. App. 89a.

Because the decision of the Court of Appeals is in direct conflict with this Court's decision in Dayton, summary reversal is appropriate. At least, this Court's review is justified.

2. The decision of the Court of Appeals rejecting Pullman abstention is a significant departure from principles previously enunciated by this Court, conflicts with the decisions of other Circuits and creates a dangerously broad exception to the doctrines of abstention.

Federal courts should not adjudicate the constitutionality of state enactments fairly open to more than one interpretation until the state courts have been afforded a reasonable opportunity to pass upon them. Harrison v. N.A.A.C.P., 360 U.S. 167, 176 (1959). Indeed, the underlying basis for Pullman abstention is the desire to avoid both unnecessary adjudication of federal questions and needless friction with state policies. Hawaii Housing Authority v. Midkiff, 467 U.S. 229, 236 (1984), citing Pullman, supra, 312 U.S. at 500.

The Court of Appeals acknowledged the existence of an unsettled question of state law, Pet. App. 59a, and it found no fault with the District Court's conclusion that a state court determination that Section 641(b) has no applicability to banks which do no business in Pennsylvania would obviate the need to address USAA's federal claims. Nevertheless, it rejected abstention under Pullman for two reasons neither of which, in our view, stand close scrutiny.

First, the court found Pullman inappropriate because one of USAA's several federal constitutional claims was a preemption claim under the Supremacy Clause which was "easily separable" from USAA's other constitutional claims (i.e., Commerce, Due Process and Equal Protection Clause claims).

Supremacy Clause claims, according to the Third Circuit, simply are not "substantial federal constitutional questions" within the meaning of Pullman. Second, the Court held that the "potential" damage that USAA's business would suffer, when weighed against Pennsylvania's interest in regulating an insurance company's ownership in lending institutions, mandated that the federal court proceed without awaiting the state court's resolution of the interpretation of Section 641. Pet. App. 59a-68. Because, as we show below, both of these rationales conflict with prior decisions of this Court and, if permitted to stand, will have a significant impact on the principles of comity and federalism which underlie abstention, the Court's review is appropriate.

a. SUPREMACY CLAUSE EXCEPTION

Noting that three "recent cases appear to reflect a growing trend," Pet. App. 64a, the Court of Appeals held that "preemption claims under the Supremacy Clause are not substantial federal constitutional issues for which Pullman abstention might be appropriate." Pet. App. 64a. This reasoning is illogical for several reasons.

USAA's constitutional claims are not limited to the Supremacy Clause; included also are Commerce, Due Process and Equal Protection Clause challenges. Pet. App. 20a, 50a. The practical effect of the Court of Appeals' rationale is that any plaintiff may defeat an otherwise appropriate abstention defense simply by appending a Supremacy Clause claim, a result clearly not envisioned

by the Pullman abstention doctrine.[12]

In Lake Carriers' Assoc. v. MacMullan, 406 U.S. 498 (1972), this Court expressly held, under circumstances similar to those present here, that abstention was appropriate when several constitutional claims, including a Supremacy Clause claim, are at issue. In Lake Carriers, plaintiffs challenged Michigan's Watercraft Pollution Control Act as being violative of the Commerce, Due Process and Equal Protection Clauses.

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[12]Furthermore, the procedural difficulties associated with the Court of Appeals' approach are obvious. What if the District Court on remand, without reaching USAA's other constitutional claims, concludes that the preemption claim is without merit? Should the question be certified for appellate review or should the Court then entertain a second motion to abstain from deciding the remaining constitutional claims?

Alleging that the state regulations also were preempted by several federal laws, the plaintiffs raised a Supremacy Clause claim. 406 U.S. at 502-503.

This Court, noting that the state law never had been construed by any Michigan court, concluded that abstention under Pullman was proper in order to determine "how far Michigan courts will go in interpreting the requirements of the state Watercraft Pollution Control Act in light of the federal Water Quality Improvement Act and the constraints of the United States Constitution." 406 U.S. at 512.[13] The Court of Appeals' holding

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[13]The Court further recognized that, by ordering abstention, the "Michigan courts may also see fit to interpret the Michigan statute in light of the other Supremacy Clause arguments that have been made in this case." Id. at 512 n.15.

here conflicts directly with this Court's decision in Lake Carriers.

In addition, the decision below conflicts with decisions from other Circuits. The First, Fourth and Seventh Circuits have concluded that Pullman abstention is appropriate when Supremacy Clause claims are at issue. See Druker v. Sullivan, 458 F.2d 1272 (1st Cir. 1972) (abstention appropriate to allow Massachusetts courts to interpret state rent control law before federal court determined whether the law applied to housing projects authorized by the National Housing Authority Act, 12 U.S.C. § 1715d); Aluminum Company v. Utilities Commission of State of North Carolina, 713 F.2d 1024 (4th Cir. 1983),

cert. denied, 465 U.S. 1052 (1984) (rejecting the view that abstention is never appropriate when plaintiff asserts a preemption claim); City Investing Co. v. Simcox, 633 F.2d 56 (7th Cir. 1982) (abstention appropriate to allow Indiana court to interpret state takeover act before federal court determined whether the enactment is preempted by the Securities Exchange Act of 1934, 15 U.S.C. § 78a).[14]

Indeed, there is no plausible reason for excluding Supremacy Clause claims from the applicability of Pullman

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[14]Interestingly, the opinion of the Court of Appeals in this case conflicts with an earlier decision of the Third Circuit. In Kennecott Corp. v. Smith, 637 F.2d 181 (3d Cir. 1980), the Court, citing Simcox, stated that "a classic situation for Pullman abstention" exists if the state law is uncertain and a finding by the state court that the statute is inapplicable would obviate the need to reach a preemption claim. 637 F.2d at 185.

abstention. As pointed out by this Court in Lake Carriers, the very purpose of abstention is to provide the state court an opportunity to reconcile state and federal enactments and thus "avoid or modify the [federal] constitutional question." 406 U.S. at 510. By so doing, the courts avoid "unnecessary friction in federal-state relations," the underlying goal of abstention. See Zwickler v. Koota, 389 U.S. 241, 249 (1967).[15]

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[15]This same overly restrictive analysis led the Court of Appeals to conclude that abstention under Burford also was inappropriate. Although the Court's reversal of Burford abstention may not, in itself, present sufficient justification for this Court's review, it does underscore the significance of the Court of Appeals' failure to implement the interests of comity and federalism which abstention is designed to promote.

Moreover, the Court of Appeals simply was incorrect in concluding that "no constitutional issues of substance are presented" in Supremacy Clause claims. Pet. App. 67a. In Hagans v. Lavine, 415 U.S. 528, 549 (1974), this Court made it clear that a preemption claim is indeed a constitutional claim. And, the adjudication of a preemption claim involves considerations of federalism, not just a simple comparison of the four corners of the state and federal statutes under review. Rather, an intent to displace state law may be evidenced in several ways and the preemption test to be applied in a given case depends upon the "dominance" of the federal government's interest. See Maryland v. Louisiana, 451 U.S. 725, 746 (1981).

For example, in Hines v. Davidowitz, 312 U.S. 52 (1941), this Court concluded that a federal statute which regulated the registration of aliens preempted any state statutes involving the same subject matter because, even though the state statutes were not necessarily inconsistent with federal law, the "regulation of aliens is so intimately blended and intertwined with responsibilities of the national government" that "the law of the state...must yield to it." 312 U.S. at 66. On the other hand, a Congressional intention to displace local laws in the exercise of the commerce power, especially where health and safety are concerned, generally is not to be inferred "unless clearly indicated" by Congress. See Maurer v. Hamilton, 309 U.S. 598, 614 (1940).

Indeed, except for those instances in which Congress has explicitly and unmistakably stated its intention to preempt an area of regulation in its entirety, a court must determine whether the state provision interferes with the federal scheme embodied in the Constitution. See San Diego Building Trades Council v. Garmon, 359 U.S. 236, 239-243 (1959). Preemption is a two step process - the first involves ascertaining the construction of the two statutes and the second involves determining the "constitutional" question whether they are in conflict. See Chicago and N.W.Tr.Co. v. Kalo Brick & Tile Co., 450 U.S. 311, 317 (1981).

Thus, because a preemption issue involves not only statutory construction, but also "profound and

delicate constitutional considerations,"[16] the Court of Appeals' holding is incorrect and calls for this Court's review.[17]

b. POTENTIAL HARM EXCEPTION

As a second reason for reversing the District Court's holding that Pullman abstention was appropriate,

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[16]See International Bros. of Electrical Workers v. Public Service Commission, 614 F.2d 206, 210 (9th Cir. 1980), citing Garmon, supra.

[17]Under Pullman abstention, the federal court does not relinquish its opportunity to determine the constitutional questions. Rather, it simply defers action pending the state court's resolution of the unsettled question of state law because that resolution may obviate the need to decide the constitutional questions. See American Trial Layers Assoc., New Jersey Branch v. New Jersey Supreme Court, 409 U.S. 467, 469 (1973). For this additional reason, there is no reason to exempt Supremacy Clause claims from Pullman applicability.

the Court of Appeals concluded that the damage which a state administrative proceeding may have on USAA's business, when weighed against Pennsylvania's interest in regulating insurance, rendered the case inappropriate for abstention. Pet. App. 62a.

These "findings" of potential damage by the Court of Appeals are no more than speculation, unsupported by the record. USAA offered no evidence in the District Court from which a conclusion may be drawn that it will suffer extraordinary harm from engaging in the administrative proceeding.[18] Moreover, as pointed out by Judge Becker in

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[18]Once the prima facie criteria for Pullman abstention are found to be present, only an "emergency situation" of grave and irreparable magnitude will justify federal court intervention. See Reetz v. Bozanich, 397 U.S. 82, 86-87 (1970); Pike v. Bruce Church Inc., 397 U.S. 137, 140 n.3 (1970).

his concurring opinion, Pet. App. 78a, this portion of the Court's holding (1) has "dangerously broad implications", Pet. App. 79a, (2) creates a precedent that could allow virtually any litigant faced with relatively complex state litigation to avoid the application of the Pullman abstention doctrine, and (3) conflicts with prior decisions of this Court which have addressed the harm sufficient to avoid Pullman abstention. See Pet. App. 80a-85a, citing Bellotti v. Baird, 428 U.S. 132, 151 (1976).

In holding as it did, the Court of Appeals ignored the fact that the case involved a garden variety administrative proceeding, and that, by virtue of the supersedeas remedies available to USAA and the Department's willingness to stay "execution in the

event of an administrative decision adverse to USAA until [state] judicial proceedings were completed," Pet. App. 60a, USSA stood in no particular danger of sustaining substantial damage during pendency of state court review. It is abundantly clear that the holding of the Court of Appeals is a significant departure from accepted judicial standards which has the practical effect of seriously weakening the Pullman abstention doctrine. This Court's review is therefore warranted. See Rule 17.1a.

CONCLUSION

The petition for writ of certiorari should be granted. Because the Court of Appeals' reversal under Younger abstention is, on its face, in direct conflict with this Court's recent decision in Dayton, the Court, without further briefing, should vacate the decision of the Court of Appeals and reinstate the district's court's dismissal based on Younger. In the alternative, following plenary review of the matter, the judgment of the Court of Appeals should be reversed.

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APPENDIX

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

UNITED SERVICES AUTOMOBILE ASSOCIATION, a Texas Reciprocal Interinsurance Exchange and USAA CASUALTY INSURANCE COMPANY, A Texas Stock Insurance Company, and USAA LIFE INSURANCE COMPANY, a Texas Stock Insurance Company, and USAA ANNUITY AND LIFE INSURANCE COMPANY, a Texas Stock Insurance Company,	:	
Plaintiffs,	:	CIVIL NO. 84-1596
vs.	:	
WILLIAM J. MUIR, III, Acting Insurance Commissioner of the Commonwealth of Pennsylvania,	:	
Defendant.	:	

MEMORANDUM

This action is a challenge to Section 641 of Pennsylvania's Insurance Department Act of 1921, 40 Pa. C.S.A. § 281. Plaintiff United Services Automobile Association and its affiliates (hereinafter U.S.A.A.) question the constitutionality of this section under

the Commerce Clause, Supremacy Clause, Due Process Clause of the Fourteenth Amendment, and Equal Protection Clause of the Fourteenth Amendment[.] Section 641 effectively prohibits any insurer who is directly or indirectly tied to a bank, public utility, savings and loan company, or the like, from doing business within the Commonwealth of Pennsylvania.

I. BACKGROUND

U.S.A.A. is a reciprocal inter-insurance exchange organized and existing under the laws of the state of Texas. Its principal place of business is in San Antonio, but it is licensed to sell insurance in Pennsylvania. In April, 1984, U.S.A.A. Financial Services, a wholly-owned subsidiary of U.S.A.A., filed an application with the Federal Home Loan Bank Board for a de novo Federal Savings Bank Charter for the U.S.A.A. Federal Savings Bank. After submission of the appropriate documents, the bank received its charter and began operations in San Antonio on December 30, 1983. This bank does no business in Pennsylvania.

In July, 1984, the Pennsylvania Insurance Department communicated to U.S.A.A. its belief that the operation of the U.S.A.A. Federal Savings Bank

placed U.S.A.A. in violation of § 641 of the Insurance Department Act. In subsequent communications, the Insurance Department advised U.S.A.A. that it must divest itself of the Bank in order to continue operating in Pennsylvania.

In October, 1984, U.S.A.A., by its attorney, responded to the Insurance Department's objections to U.S.A.A.'s indirect acquisition of the Bank and offered an interpretation of § 641 that did not prohibit such an affiliation. When the Insurance Department continued to maintain that U.S.A.A. was in violation of § 641, U.S.A.A. instituted this action against the Acting Insurance Commissioner for a declaratory judgment that § 641 is unconstitutional as applied to U.S.A.A.'s ownership of the Bank and for an injunction against enforcement of § 641 against U.S.A.A.

Defendant responded on December 24, 1984 by moving to dismiss the complaint or stay the proceedings on the ground that the federal courts should abstain from deciding this issue. On the same day, the Insurance Department issued an Order to Show Cause, directing plaintiffs to appear at an administrative hearing for the purpose of determining whether or not plaintiffs have violated § 641(b) of the Insurance Department Act. Plaintiffs opposed the abstention motion and, on January 25, 1985, filed their own motion for summary judgment on preemption grounds. Both of these motions are now before us, but because we find that defendant's abstention motion has merit, we do not reach the preemption issue.

II. ABSTENTION

In certain situations, a federal court may be justified in refusing to exercise its jurisdiction over a cause of action, even though jurisdiction may exist under the constitution and appropriate statutes. Such refusal to exercise jurisdiction is labelled abstention. The abstention doctrine is really a collection of four different doctrines, all concerned with comity, but each deriving from a seminal Supreme Court case and each serving slightly different purposes. The four doctrines are (1) the so-called Pullman doctrine, derived from Railroad Commission of Texas v. Pullman, 312 U.S. 496 (1941); (2) the Burford doctrine, derived from Burford v. Sun Oil Co., 319 U.S. 315

(1943); (3) the Younger v. Harris doctrine derived from Younger v. Harris, 401 U.S. 37 (1971); and (4) the Colorado River Water Conservation District doctrine, derived from Colorado River Water Conservation District v. United States, 424 U.S. 800 (1976).

In the case presently before us, defendant asserts that there are two types of abstention applicable, and we believe that as many as three support our dismissal of this action. These three are the Pullman, Burford, and Younger doctrines. We will address each doctrine in turn.

A. Pullman Abstention.

Pullman abstention is exercised by federal courts when, along with the constitutional issue in a case, there is an important state law issue which is unclear, and when prompt resolution of

the unsettled state law question will likely avoid the need for a constitutionally-based decision. The Supreme Court first developed and applied this doctrine in Railroad Commission of Texas v. Pullman, supra. In that case, the Texas Railroad Commission had ordered that Pullman sleeping cars must be attended at all times by a conductor, rather than a porter as was the custom of less travelled routes. The Commission's order had a racially discriminatory effect, because all conductors were white, while all porters were black.

In exercising Pullman - type abstention for the first time, the Supreme Court noted that the purpose of such restraint was to demonstrate "'scrupulous regard for the rightful independence of the state governments' and for the smooth working of the federal

judiciary." Pullman, 312 U.S. at 501. In Pullman, abstention was warranted because, along with the "substantial constitutional issue" (race discrimination) touching on "a sensitive area of social policy upon which the federal courts ought not to enter unless no alternative . . . is open," id. at 498, there was a question of the statutory authority of the Railroad Commission to promulgate the discriminatory regulation. Because the law of Texas furnished "easy and ample means for determining the Commission's authority," id. at 501, and because the constitutional adjudication could plainly be avoided "if a definitive ruling on the state issue would terminate the controversy," id. at 498, the Supreme Court ruled that it was appropriate for the district court to stay the federal

proceeding pending resolution of the state issue in the state court.

In cases subsequent to Pullman, the Supreme Court and the lower federal courts fleshed out this doctrine, making it clear that this doctrine of abstention

> is an extraordinary and narrow exception to the duty of a District Court to adjudicate a controversy properly before it. Abdication of the obligation to decide cases can be justified under this doctrine only in the exceptional circumstances where the order to the parties to repair to the state court would clearly serve an important countervailing interest.

County of Allegheny v. Frank Mashuda Company, 360 U.S. 185, 188-189 (1959). Despite the narrowness of the doctrine, abstention is quite proper "when difficult and unsettled questions of state law

must be resolved before a substantial federal constitutional question can be decided." Hawaii Housing Authority v. Midkiff, 81 L.Ed.2d 186, 194 (1984).

The overriding prerequisite to exercise of Pullman abstention appears, from the case law, to be that the state law question be "unsettled" and potentially dispositive. The Supreme Court has stated,

> The relevant inquiry is not whether there is a bare, though unlikely, possibility that state courts might render adjudication of the federal question unnecessary. Rather, "[w]e have frequently emphasized that abstention is not to be ordered unless the statute is of an uncertain nature, and is obviously susceptible of a limiting construction."

Hawaii Housing Authority, supra, at 195, quoting Zwickler v. Koota, 389 U.S. 241, 251 (1967).

The instant case is one in which there is clearly an unsettled and potentially dispositive issue of state law. The dispute between U.S.A.A. and the Insurance Department has, from the beginning, focused on the interpretation of § 641 of the Insurance Department Act. The Insurance Department relies on subsection (b) to support its mandate that U.S.A.A.'s affiliation with the U.S.A.A. Federal Savings Bank must be severed if U.S.A.A. is to retain its license to sell insurance in Pennsylvania. U.S.A.A. on the other hand, relies on subsections (c) and (a)(1) in arguing that the Insurance Department's interpretation of the Act is erroneous and that it need not divest itself of the Bank.

The language relied on by the Insurance Department, in pertinent part, reads "[N]o lending institution, public utility, bank holding company, savings and loan holding company, or any subsidiary or affiliate of the foregoing, . . . may, directly or indirectly, be licensed or admitted as an insurer or be licensed to sell insurance in this State . . . ." 40 Pa. C.S.A. § 281(b). In its enforcement communications with U.S.A.A., the Insurance Department apparently assumed that U.S.A.A. is a bank holding company. Bank holding companies, no matter where their banks are located, are barred from holding an insurance license in Pennsylvania, according to the Insurance Department's interpretation of this section.

Although this interpretation of § 641(b) appears to flow naturally from the clear language of subsection (b), an ambiguity arises when § 641 is read as a whole. Subsection(c) states the purposes of § 641:

> to help maintain the separation between lending institutions and public utilities and the insurance business and to minimize the possibilities of unfair competitive practices by lending institutions and public utilities against insurance companies, agents and brokers.

40 Pa. C.S.A. § 281(c). "Lending institution" as used in subsection (c), and, indeed, in the whole of § 641, is defined as "any institution that accepts deposits and lends money in the Commonwealth of Pennsylvania...." 40 Pa. C.S.A. § 281(a)(1). Given this definition of lending institution as limited to institutions accepting deposits and lending money in Pennsylvania, the clearly stated purpose of § 641 then, is

to maintain separation between Pennsylvania lending institutions and the insurance business.

The Insurance Department's purportedly clear meaning interpretation of § 641(b) simply does not mesh with the clearly stated purpose of the section as expressed in § 641(c). In fact, as applied to U.S.A.A. and the U.S.A.A. Federal Savings Bank, a Texas lending institution, there is a blatant conflict between the stated purpose of § 641 and the result reached by literal application of subsection (b) to the instant situation. This conflict between subsections (b) and (c) is just the type of ambiguity that triggers the application of Pullman abstention. As confirmed by the Third Circuit in a recent ruling, abstention is appropriate even in a case where, as here, the ambiguity appears only when two otherwise clear statutory

provisions are read side by side: "The need for state court interpretation results not only from unclear language on the face of a single statute, but also from the juxtaposition of clear, but contradictory state provisions." Georgevich v. Strauss, No. 84-5194, slip. op. (3d Cir., September 5, 1985).

Once it is established that an ambiguity exists sufficient to call for application of the Pullman abstention doctrine, the district court must next determine whether resolution of the state law will avoid the need for a constitutionally-based decision. In this case, decision of the state law question is a logical prerequisite to consideration of U.S.A.A.'s constitutional challenges. If a court were to determine that the clearly articulated

purpose of § 641(c) controls the interpretation of § 641(b), then U.S.A.A. would not be in violation of the statute and there would be no need to reach the constitutional issues.

Because we have determined that a potentially dispositive issue of state law exists, we must turn to the final consideration involved in Pullman abstention questions: are there the requisite "exceptional circumstances" and would abstention "clearly serve an important . . . interest"? See County of Allegheny v. Frank Mashuda Company, supra, at 189. In other words, are there considerations of comity that would mandate state court, rather than federal court, decision of the state law issue? The answer in this case is yes. Under the McCarran-Ferguson Act, 15 U.S.C. § 1011-1105, power to regulate

the insurance industry was given exclusively to the states. The ambiguous state statute in question is part of a comprehensive regulatory scheme implementing the power granted under the McCarran-Ferguson Act. Interpretation of such a statute and resolution of ambiguities therein should be left, therefore, in the first instance, to the state administrative machinery and eventually through appeals, to the state court system. Accord, Mathias v. Lennon, 474 F.Supp. 949 (S.D. N.Y. 1979)("Not only would the New York court's decision have special authority on questions of New York law, but it undoubtedly possesses greater experience in dealing with the highly technical insurance statutes involved here." Id. at 95556 [sic-956]).

U.S.A.A. argues that we should not abstain in this case because of the delays inherent in abstention and because of the resulting prejudice to U.S.A.A. and its policyholders. U.S.A.A. claims that, if the state administrative and court system is permitted to decide the state law issue, U.S.A.A. will be deprived of its license to sell insurance in this state pending final adjudication of the constitutional claims. We do not agree with the conclusion that U.S.A.A. will be deprived of its license to its prejudice. Even assuming that the state courts fail to decide the state law issue in U.S.A.A.'s favor, U.S.A.A. will suffer no prejudice because of the availability of appeal and supersedeas procedures. These procedures will assure U.S.A.A. that, before its license is revoked and it is

prohibited from doing business in Pennsylvania, it will have the opportunity to be heard on both the state law issue and the constitutional challenges.

U.S.A.A. also objects to abstention on the ground that abstention is inappropriate where the constitutional issue is a preemption claim based on the Supremacy Clause. We cannot accept this contention in this case because preemption is not the only constitutional claim raised in the complaint, as U.S.A.A. should know.

B. Burford Abstention.

The second type of abstention applicable to this case is that exercised in Burford v. Sun Oil Company, 319 U.S. 315 (1943). In that case, the Texas Railroad Commission granted Burford a permit to drill four wells.

Sun Oil brought an action in district court attacking the validity of the order granting the permit. In ruling that the federal courts should not involve themselves in essentially regulatory matters, the Supreme Court noted the confusion caused by such intervention:

> The very "confusion" which the Texas legislature and Supreme Court feared might result from review by many state courts of the Railroad Commission's orders has resulted from the exercise of federal equity jurisdiction... . Delay, misunderstanding of local law and needless federal conflict with the State policy, are the inevitable product of this double system of review.

Burford, supra, at 327. In light of the problems inherent in the exercise of federal court jurisdiction over state regulatory matters when there is an

extensive and complicated regulatory scheme, the Supreme Court held that abstention was the most appropriate course of action:

> The State provides a unified method for the formation of policy and determination of cases by the Commission and by the state courts. The judicial review of the Commission's decisions in the state courts is expeditious and adequate. Conflicts in the interpretation of state law, dangerous to the success of state policies, are almost certain to result from the intervention of the lower federal courts. On the other hand, if the state procedure is followed from the Commission to the State Supreme Court, ultimate review of the federal questions is fully preserved here... . Under such circumstances, a sound respect for the independence of state action requires the federal equity court to stay its hand.

Id. at 333-34.

From the language of the Supreme Court in Burford, and in other cases raising similar issues, it appears that the central requirement for the exercise of Burford abstention is the existence of "difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar." Colorado River Water Conservation District v. United States, 424 U.S. 800, 814 (1976); Accord, County of Allegheny v. Frank Mashuda Company, 360 U.S. 185, 189 (1959)("This Court has also upheld an abstention on grounds of comity with the States when the exercise of jurisdiction by the federal court would disrupt a state administrative process, ... or otherwise create needless friction by unnecessarily enjoining state officials from executing domestic policies...").

These types of state law questions bearing on important state issues have been recognized in a variety of contexts, including insurance regulation cases. In Levy v. Lewis, 635 F.2d 960 (2d Cir. 1980), the Second Circuit ruled that a dispute between retired employees of Consolidated Mutual Insurance Company and the liquidator of that company should have been left to the state administrative and court systems for determination. In applying Burford abstention, the court noted that "the federal courts have abstained in numerous areas where state regulation involved matters of substantial state concern and where state policies were carried out in a statutorily established regulatory program by state officials." The court found that the area of insurance regulation was an area in which

state court and administrative systems deserved great deference by federal courts:

> It is ... highly significant that the state scheme has been adopted pursuant to congressional authorization. In the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1105, Congress mandated that regulation of the insurance industry be left to the individual states. Thus, the administrative and judicial scheme erected by New York to regulate insurance companies, including that part enabling institution and implementation of liquidation proceedings, operates pursuant to an express federal policy of noninterference in insurance matters. Federal courts have therefore been slow to interpret such schemes unless necessary, particularly when federal court action would impinge upon the area in which Congress has recognized the overriding interest of the states.

Levy, supra, at 963-964.

We find that Burford abstention is appropriate in this case not only because we agree with the Second circuit in Levy that federal courts should be slow to disrupt state insurance regulatory schemes authorized by the McCarran-Ferguson Act, but also because of the extensive and complicated nature of the state regulatory scheme involved. The policies implemented by § 641 of the Pennsylvania Insurance Department Act are essentially state policies developed to protect state citizens and implement state concerns. As in Burford itself, the state in this case provides a "unified method for the formation of policy and determination of cases by the commission and by the state courts." Burford, supra, at 333.

If the state procedure is followed from the Insurance Department up through the Commonwealth Court and the State Supreme Court, the state itself will have an opportunity to interpret and mold its own policies in this area of significant state concern, while at the same time, the federal questions will be preserved for ultimate review by the United States Supreme Court, if necessary. No disruption of the State administrative procedures will be necessary, and the potential for conflicting and confusing federal court and state court rulings will disappear.

We do not agree with U.S.A.A.'s argument that abstention is inappropriate because the factual situation presented here does not involve the "business of insurance" and therefore is not governed by the McCarran-Ferguson

Act. Even if § 641 does not directly regulate an "integral part of the policy relationship between the insurer and the insured," Union Labor Life Insurance Co. v. Pireno, 458 U.S. 119, 129 (1982), the policies behind § 641 and designed to be implemented by § 641 may have everything to do with the relationship between insurers and insured. Formulation and implementation of such policies are strictly the province of the state's legislative and administrative bodies. To avoid federal interference in such an important area of state functioning, we must abstain from exercising our jurisdiction in this case.

We also do not agree that Burford abstention is inappropriate because the administrative proceeding in this case was instituted the same day as the motion to dismiss was filed. It is not a requirement of Burford abstention

that there be a specific preexisting state proceeding to which the federal court may defer.[1] Rather, all that is required is that there be a pervasive regulatory scheme and a procedure within that scheme through which plaintiff's complaints may be addressed. See Meicler v. Aetna Casualty and Surety Company, 372 F.Supp. 509 (S.D. Texas 1974), aff'd, 506 F.2d 732 (5th Cir. 1975).

C. Younger Abstention.

The final abstention doctrine applicable to this case is the one derived from the Younger v. Harris case and its progeny. Although none of the parties in the instant case argued the

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[1]Such a proceeding is required when exercising Younger abstention, however. This requirement will be discussed further in section C, infra.

merits of this doctrine in connection with the motion before us now, our review of the case law on abstention indicates that this third type of abstention is also applicable.

Younger abstention, originally a doctrine applicable only to actions brought in a federal court to enjoin state criminal proceedings, has broadened in recent years to include even federal actions to enjoin ongoing state administrative proceedings. See, Williams v. The Red Bank Board of Education, 662 F.2d 1008 (3d Cir. 1981). As noted by the Third Circuit in that case, the keystone of the Younger abstention doctrine is

> the notion of "comity," that is, a proper respect to state functions, a recognition of the fact that the entire country is made up of a Union of separate state

> governments, and a continuance of the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways.

Id. at 1014, quoting Younger v. Harris, 401 U.S. 37, 44 (1971).

According to the Third Circuit's reading of the Younger doctrine in the Williams case, Younger abstention is appropriate "where federal intervention into state administrative proceedings would be substantial and disruptive, and where the state proceedings are adequate to vindicate federal claims and reflect strong and compelling state interest." Id. at 1077. A prerequisite to such abstention, of course, is that there be an existing state proceeding

to which the federal court may defer. Hawaii Housing Authority v. Midkiff, 81 L.Ed.2d 186, 195 (1984).

In the instant case the state administrative proceeding was instituted after U.S.A.A. filed its complaint in this court. The bare fact that the state proceeding came after the initial filing in federal court does not render Younger abstention inapplicable, however. The Supreme Court stated in the Hawaii Housing Authority case that Younger abstention is appropriate "when state court proceedings are initiated 'before any proceedings of substance on the merits have taken place in the federal court.'" Id. at 195, quoting Hicks v. Miranda, 422 U.S. 332, 349 (1975). The state Order to Show Cause was issued by the Insurance Department in the instant case on the same day that

defendant filed his motion to dismiss in federal court. This motion to dismiss was the first motion filed in the case. We do not believe that the mere filing of a motion means that proceedings of substance on the merits have taken place in federal court. Further, although the Order to Show Cause was not issued until December 24, 1984, the administrative enforcement machinery began rolling in July and August, 1984 when the Insurance Department formally communicated to U.S.A.A. its belief that U.S.A.A. was in violation of § 641.

Given that we find that there is a preexisting state administrative proceeding, we must next engage in the two-step analysis of the propriety of abstention recommended by the Third Circuit in Williams. The first step is to determine if the state's interest in going forward with the administrative

proceeding without intrusion by the federal courts is sufficiently weighty to mandate Younger abstention. Williams, 662 F.2d at 1017. As noted in the prior analyses of the other types of abstention, the state's interest in regulating the insurance industry is a substantial one. Pennsylvania has established an extensive and comprehensive scheme for regulating the licensure and operations of insurance companies in this Commonwealth. Regulation of the insurance industry is committed solely to the states by the McCarran-Ferguson Act. Any intervention into this regulatory process by a federal court should not be taken lightly. Because insurance regulation is solely the concern of the states, and because Pennsylvania has implemented an extensive scheme for that regulation, we find that Pennsylvania's

interest in going forward with the administrative proceeding is sufficiently weighty to justify abstention under the Younger doctrine.[2]

The second prerequisite to the application of Younger abstention is that there be a state administrative forum adequate to vindicate the federal or constitutional claims raised by plaintiff. As we have already noted,

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[2]Mathias v. Lennon, 474 F.Supp. 949 (S.D. N.Y. 1979), another district court case, also held that Younger abstention was appropriate in the context of an insurance dispute where there was a preexisting administrative proceeding. In that case the court said "[t]he fact that this case seeks to enjoin a ruling in a pending state proceeding, brought by a state official, implicating an important state concern and in which Mathias is fully able to raise the constitutional claims made here strongly supports the conclusion that the complaint should be dismissed." Id. at 956.

Pennsylvania provides such a forum through its system of appeals to the Commonwealth Court and the state Supreme Court.

Because we find that the instant case meets all the prerequisites for Younger abstention, and because it involves regulation of the insurance business which is committed to the states, we hold that Younger abstention is appropriate in this case.

The appropriate procedure when a district court abstains from deciding a case or an issue more appropriately handled by the state courts is either a stay of the federal court proceedings or dismissal of the case from federal court altogether, depending upon the type of abstention exercised and a "consideration of what is appropriate to the cir-

cumstances of that case." Williams v. The Red Bank Board of Education, supra, at 1023, n. 15. Because we find today that the state administrative and court systems provide an opportunity for U.S.A.A. to raise all of its claims, and because successful pursuit of those claims in the state system will afford U.S.A.A. all of the relief it requests from this court, we will dismiss the action on abstention grounds.

/s/ R. DIXON HERMAN
UNITED STATES DISTRICT JUDGE

DATED: Sept. 30, 1985

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

UNITED SERVICES AUTOMOBILE ASSOCIATION, a Texas Reciprocal Interinsurance Exchange and USAA CASUALTY INSURANCE COMPANY, A Texas Stock Insurance Company, and USAA LIFE INSURANCE COMPANY, a Texas Stock Insurance Company, and USAA ANNUITY AND LIFE INSURANCE COMPANY, a Texas Stock Insurance Company,	:	
Plaintiffs,	:	CIVIL NO. 84-1596
vs.	:	
WILLIAM J. MUIR, III, Acting Insurance Commissioner of the Commonwealth of Pennsylvania,	:	
Defendant.	:	

O R D E R

AND NOW, this 30th day of September, 1985, IT IS ORDERED that Defendant's motion to dismiss be and hereby is granted.

The Clerk of Court is directed to close the file.

/s/ R. DIXON HERMAN
UNITED STATES DISTRICT JUDGE

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 85-5662

UNITED SERVICES AUTOMOBILE ASSOCIATION,
a Texas Reciprocal Interinsurance
Exchange

and

USAA CASUALTY INSURANCE COMPANY,
a Texas Stock Insurance Company

and

USAA LIFE INSURANCE COMPANY,
a Texas Stock Insurance Company

and

USAA ANNUITY AND LIFE INSURANCE COMPANY
a Texas Stock Insurance Company

v.

WILLIAM J. MUIR, III,
Acting Insurance Commissioner of the
Commonwealth of Pennsylvania

United Services Automobile
Association, USAA Casualty Insurance
Company, USAA Life Insurance
Company, and USAA Annuity and Life
Insurance Company,
Appellants

Appeal from the United States District
Court for the
Middle District of Pennsylvania
(Scranton)
Civil No. 84-1596

Argued March 6, 1986
Before GIBBONS, BECKER, and ROSENN,
Circuit Judges
Opinion Filed June 6, 1986

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OPINION OF THE COURT

ROSENN, Circuit Judge

This appeal requires us to examine various forms of abstention advanced by the district court in choosing to refrain from exercising jurisdiction. Included is an unsettled question under the abstention doctrine promulgated in Railroad Commission of Texas v. Pullman, 312 U.S. 496 (1941): whether a claim that federal statutes preempt state law under the supremacy clause raises a substantial constitutional question which permits abstention.

United Services Automobile Association (USAA) and some of its subsidiary insurance companies filed suit against William J. Muir, III, as Acting

Insurance Commissioner of the Commonwealth of Pennsylvania, seeking to enjoin the state insurance department from revoking USAA's license to insure persons in Pennsylvania. The insurance department asserts that USAA following its purchase of a Texas bank is in violation of a Pennsylvania statute prohibiting mergers between financial institutions and insurers. USAA argues that such a construction of the state statute is preempted by federal banking statutes that permitted it to purchase the bank and otherwise violates the constitution. The United States District Court for the Middle District of Pennsylvania concluded that abstention

applied, and dismissed the suit.[1] We disagree and reverse.

I.

The relevant facts as stated in USSA's complaint are not disputed in this appeal. USAA is a reciprocal interinsurance exchange[2] organized

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[1]The district court had jurisdiction under 28 U.S.C. § 1331 (1982) (federal questions), 28 U.S.C. § 1332 (1982)(diversity), and 28 U.S.C. § 1337 (1982) (statutes affecting commerce). For diversity purposes, USAA and its subsidiaries are residents of Texas, and Muir is a resident of Pennsylvania. Dismissal following an abstention order is a final judgment reviewable by this court under 28 U.S.C. § 1291 (1982). Baltimore Bank for Cooperatives v. Farmers Cheese Cooperative, 583 F.2d 104, 109 (3d Cir. 1978).

[2]In a reciprocal interinsurance exchange,

> individuals, partnerships, or corporations engaged in a similar line of business undertake to indemnify each

(FOOTNOTE CONTINUED ON NEXT PAGE)

under the laws of Texas. USAA and three of its wholly owned insurance company subsidiaries, with which it filed this suit, have their principal place of business in San Antonio, Texas. They limit their insurance services primarily to commissioned officers of the United States armed forces and do business nationwide. They provided insurance services in 1983 to more than 40,000 Pennsylvania policy holders who paid more than $35,000,000 in annual policy premiums.

(FOOTNOTE CONTINUED)

other against a certain kind or kinds of losses by means of mutual exchange of insurance contracts. . . . whereby each member separately becomes both an insured and an insurer with several liability only.

2 Couch on Insurance, § 18:11 at 614-15 (2d ed. 1984).

That year, USAA Financial Services Company (then known as USAA Development Company), a wholly owned subsidiary of USAA, applied for and received from the Federal Home Loan Bank Board and the Federal Savings & Loan Insurance Corporation (FSLIC) permission to organize and operate the USAA Federal Savings Bank (the Bank) in San Antonio, Texas. USAA Financial Services also received permission from the FSLIC to serve as a unitary savings and loan holding company. The insurance department does not allege that USAA failed to comply with any requirements of federal law in organizing the Bank. USAA has made an initial investment of more than $20,000,000 through its subsidiary to capitalize the Bank. The subsidiary holding company and the Bank are not

parties to this suit. The Bank does not solicit deposits from Pennsylvania residents or do business in Pennsylvania.

In mid-1984, the Pennsylvania insurance department notified USAA that its ownership of a bank violated section 641 of the Pennsylvania Insurance Act of 1921, and that "USAA must, to continue its business in Pennsylvania, divest itself of the Bank, or, failing such divestiture, risk revocation of its license to transact insurance business in Pennsylvania." The Pennsylvania Insurance Act of 1921, section 641, as amended in 1974, provides in relevant part:

(b) No lending institution, . . . bank holding company, savings and loan holding company [as defined in federal statutes] or any subsidiary or affiliate of the foregoing, or officer or employee thereof, may directly or indirectly, be licensed or admitted as an insurer . . . in this State . . . .

(c) The Insurance Commissioner is authorized to promulgate regulations in order to effectuate the purposes of the section, which are to help maintain the separation between lending institutions and public utilities and the insurance business and to minimize the possibilities of unfair competitive practices by lending institutions . . . against insurance companies, agents and brokers.

Codified at 40 Pa. Stat Ann. § 281 (Purdon 1985 Supp.).

The insurance department argued that because USAA Financial Services is a federally regulated savings and loan holding company, as defined by federal statutes, and solely owns USAA Financial Services, the latter is its affiliate and USAA is therefore in violation of section 641(b). In reply, USAA asserted that section 641 is ambiguous and can be read not to apply to it. Section 641(c) states that the purpose of section 641 is to help maintain the separation between lending institutions and the insurance business and minimize the possibilities of unfair competitive practices by lending institutions. Under section 641(a)(1),[3] a lending

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[3]Section 641(a)(1) provides:
(a) As used in this section [641]:

(FOOTNOTE CONTINUED ON NEXT PAGE)

institution means any institution that does banking business in Pennsylvania. By reading parts (a)(1) and (c) of section 641 together, USAA argued that the purpose of the section is limited to preventing financial institutions doing business in Pennsylvania from competing or being affiliated with Pennsylvania insurers; as the Bank is based and does business only in Texas, the section does not apply to USAA.

(FOOTNOTE CONTINUED)

> (1) "Lending institution" means any institution that accepts deposits and lends money in the Commonwealth of Pennsylvania, including banks and savings and loan associations, but excluding insurance companies.

Codified at 40 Pa. Stat. Ann. § 281(a)(1)(emphasis added).

USAA and its plaintiff subsidiaries filed suit in the district court under 42 U.S.C. § 1983, alleging that the insurance department's proposed reading of section 641 violated the supremacy, equal protection, and due process clauses of the constitution, and seeking declaratory and injunctive relief. One month after USAA filed suit, the insurance department commenced state administrative proceedings for the revocation of USAA's insurance licenses in Pennsylvania and filed in the district court a motion to dismiss the suit on abstention grounds. While the district court considered this motion, USAA filed a motion for summary judgment on preemption grounds. Citing Pullman, supra, Burford v. Sun Oil Co., 319 U.S. 315 (1943), and Younger v. Harris, 401

U.S. 37 (1971), the district court concluded that it should abstain from addressing USAA's suit, and dismissed the suit without considering USAA's summary judgment motion. USAA appealed.

On November 22, 1985, this court granted a motion for an injunction preventing the insurance department from revoking USAA's licenses pending resolution of this appeal. The Pennsylvania Insurance Commissioner has heard testimony in the administrative proceedings to revoke USAA's licenses, but, as of oral argument, he had not announced any decision.

II.

Abstention from the exercise of federal jurisdiction is, in all its forms, "the exception, not the rule." Colorado River Water Conservation District v. United States, 424 U.S. 800,

813 (1976). It is an extraordinary and narrow exception to the district court's duty to adjudicate a controversy properly before it, justified only in the exceptional circumstances where resort to state proceedings clearly serves an important countervailing interest. Id.

In reviewing abstention decisions, appellate courts apply the various criteria for abstention articulated by the Supreme Court in much the same way they would apply provisions of a statute. 1A J. Moore, Federal Practice § 0.203[1] at 2106 (1985). A district court has little or no discretion to abstain in a case that does not meet traditional abstention requirements. C-Y Development Co. v. City of Redlands, 703 F.2d 375, 377 (9th Cir. 1985). Within these constraints, determination whether the exceptional circumstances required for abstention exist is left

to the district court, and will be set aside on review only if the district court has abused its discretion. Harman v. Forssenius, 380 U.S. 528, 534 (1965); United States v. City of Pittsburgh, 757 F.2d 43, 45 (3d Cir. 1985). Determinations that are essentially legal, such as deciding whether interpretation of a state law is unsettled, are reviewed do novo on appeal. D'Iorio v. County of Delaware, 592 F.2d 681, 686 (3d Cir. 1978). overruled on other grounds, Kershner v. Mazurkiewicz, 670 F.2d 440 (3d Cir. 1982) (in banc). We therefore turn to an analysis of the abstention grounds on which the district court relied.

III.

Pullman abstention, as most recently defined by the Supreme Court, instructs "that federal courts should abstain from decision when difficult and unsettled questions of state law must be resolved before a substantial federal constitutional question can be decided." Hawaii Housing Authority v. Midkiff, 467 U.S. 229, 236 (1984). USAA advances three principal grounds for not applying Pullman abstention in this case: there is no unsettled question of state law; abstention would cause USAA substantial and irreparable economic harm; and its preemption claim does not constitute a substantial federal constitutional question.

A.

For Pullman to apply, the state statute must be "obviously susceptible of a limiting construction" and "a bare, though unlikely, possibility that state courts might render adjudication of the federal question unnecessary" is insufficient. Hawaii Housing, 467 U.S. at 237 (emphasis in original). A statute is unsettled for Pullman purposes when two of its provisions are contradictory. Georgevich v. Strauss, 772 F.2d 1078, 1090-91 (3d Cir. 1985) (in banc), cert. denied, 106 S.Ct. 1229 (1986). In seeking Pullman abstention, the insurance department has argued that the provisions of section 641 are ambiguous and contradictory, and that with no state court decisions interpreting the section, its meaning is unsettled. In reply, USAA contends that the insurance

department's interpretation of the laws it is charged with enforcing and its actions implementing that interpretation renders the statute unambiguous.

The Supreme Court has held that Pullman abstention is not appropriate if an otherwise ambiguous statute has been authoritatively construed by the state courts, see e.g. Kusper v. Pontikes, 414 U.S. 51, 55-56 (1973), but it has not held that an administrative interpretation will suffice as an authoritative reading of state law. Although one court has suggested that an administrative interpretation of a statute that creates a constitutional problem eliminates the statute's ambiguity, the challenged statute in that case was clear on its face and not susceptible of any other construction. National City Lines, Inc. v. LLC Corp., 687 F.2d 1122,

1126 (8th Cir. 1982). Indeed, an administrative interpretation that would moot the constitutional issue raised by another reading of an ambiguous statute fortifies the claim for abstention. See, e.g., Bellotti v. Baird, 428 U.S. 132, 148 (1976); Georgevich, 772 F.2d at 1090-91.

Generally, an administrative interpretation of a facially ambiguous state statute will not remove the ambiguity, for Pullman purposes. See Anderson v. Babb, 632 F.2d 300, 306 (4th Cir. 1980). In keeping with statutorily imposed maxims for construing legislative intent, Pennsylvania courts ordinarily defer to administrative interpretations of statutes. See 1 Pa. Cons. Stat. Ann. § 1921(c)(8) (Purdon 1985 Supp.). The interpretation given a statute by the agency charged with its execution and application "is entitled

to great weight and should be disregarded or overturned only for cogent reasons or if such construction is clearly erroneous." Cohen v. Pennsylvania Public Utility Commission, 494 A.2d 58, 61 (Pa. Comm. Ct. 1985); see Wiley House v. Scanlon, 465 A.2d 995, 999 (Pa. 1983) (administrative interpretation of a regulation followed unless it is plainly erroneous or inconsistent with the authorizing statute). Although the insurance department's interpretation of section 641 is not clearly erroneous, USAA's cogent alternative interpretation that the statute does not apply to lending institutions that do not do business in Pennsylvania might well be adopted by the state courts. Thus, despite the deference Pennsylvania courts pay administrative interpretations, we cannot say that they would accept the insurance department's

interpretation of section 641 as a definitive statement of Pennsylvania law. The state law is therefore unsettled for Pullman purposes.

B.

USAA also argues that the potential damage that its business would suffer during state administrative and court proceedings outweighs any important countervailing interests of Pennsylvania in abstention. The Supreme Court has held that a district court was fully justified in not abstaining when the constitutionality of a narrow and specific-- though ambiguous -- state statute was at issue, and any delay in settling the issue would result in substantial economic losses. Pike v. Bruce Church Inc., 397 U.S. 137, 140 & n.3 (1970)(allegedly unconstitutional state regulation threatened loss of $700,000

fruit crop. This court observed that undue delay and the increased cost of state litigation made abstention unnecessary when the federal court in resolving the constitutional issue "would not upset sensitive state programs" and the issue was neither novel nor difficult. McKnight v. Southeastern Pennsylvania Transportation Authority, 583 F.2d 1229, 1241 (3d Cir. 1978) (narrow due process rights of certain state employees facing dismissal). The Court, however, did not find that the district court abused its discretion by abstaining. Id. at 1242.

The insurance department has indicated a willingness to expedite consideration of USAA's claims in state procedures, and to agree to a stay of execution in the event of an administrative decision adverse to USAA until judicial proceedings were completed. USAA

explains plausibly, however, how a state administrative order to revoke its insurance license, even if stayed, would in itself hurt its reputation generally and impair its marketing of insurance, even in other states, regardless of the time factor in litigating. It is uncontested that USAA has an excellent nationwide reputation as an insurer and is financially sound. The threat of a license revocation, a harsh sanction, may suggest in the marketplace fraudulent or illegal activity or financial instability. It could be difficult or perhaps impossible for USAA to explain to consumers and to the insurance industry that the license revocation proceedings in Pennsylvania do not represent such a sanction. The threat of revocation might alarm an unknown number of USAA's more than 40,000 Pennsylvania policyholders into cancelling

their insurance. Nationwide, a revocation order even if stayed, would prevent USAA from continuing unqualifiedly to represent that its insurance contracts are available in all 50 states. Because USAA limits its policies primarily to commissioned officers of the United States armed forces, persons who move frequently in the service of their country, the inability to offer insurance coverage in every state may well be a major blow.

Weighing the legal issues and the devastating economic consequences a license revocation would impose upon USAA on the one hand and the vague claim of risks to the state from a Texas bank not doing business in Pennsylvania on the other hand, we conclude that the district court erred by holding that state appeal and supersedeas procedures adequately protected USAA's interests.

See Professional Plan Examiners of New Jersey v. Lefante, 750 F.2d 282, 290-91 (3d Cir. 1984).

C.

Alternatively, USAA asserts that its claim that federal statutes preempt contrary state insurance laws does not pose the substantial federal constitutional claim required for Pullman abstention. Hawaii Housing, 467 U.S. at 236. The Ninth Circuit supports this claim for it has held that Pullman abstention is inappropriate for preemption questions grounded in the Supremacy Clause. Knudsen Corp. v. Nevada State Dairy Commission, 676 F.2d 374, 377 (9th Cir. 1982). "Although preemption has its doctrinal base in the Constitution, the question is largely one of determining the compatibility of a state and

a federal statutory scheme. No constitutional issues of substance are presented." Id. The Tenth Circuit recently reached the same conclusion, stating in strong dictum that "[t]he Supreme Court does not appear to view federal preemption questions based only on the Supremacy Clause as the type of constitutional issues that the Pullman doctrine counsels courts to avoid." Federal Home Loan Bank Board v. Empie, 778 F.2d 1447, 1451 n.4 (10th Cir. 1985); see International Longshoremen's Association, AFL-CIO v. Waterfront Commission of New York Harbor, 495 F.Supp. 1101, 1113-14 & nn.51-18 (S.D.N.Y. 1980), modified in other part, 642 F.2d 666 (2d Cir.), cert. denied, 454 U.S. 966 (1981). These recent cases appear to reflect a growing trend.

This court recently has also suggested in dicta that preemption questions are not appropriate for Pullman abstention. In reversing a district court abstention decision, we stated that "[i]t would be inconsistent with our paramount duty to interpret and protect federal law to invoke Pullman abstention in this preemption case." Kennecott Corp. v. Smith, 637 F.2d 181, 185 (3d Cir. 1980). Supremacy clause claims essentially involve federal policy and "the federal courts are particularly appropriate bodies for the application of preemption principles." Id. (quoting Hagans v. Lavine, 415 U.S. 528, 550 (1974)). Because the questioned state statute in Kennecott unambiguously conflicted with the federal statute, there was no unsettled state law question requiring Pullman abstention. 637 F.2d at 185.

The Supreme Court has held that "the basic question involved in [preemption claims under the Supremacy Clause] is never one of interpretation of the Federal Constitution but inevitably one of comparing two statutes," Swift & Co. v. Wickham, 382 U.S. 111, 120 (1965), and where a case involves a nonconstitutional federal issue, the necessity for deciding which depends on the decision of an underlying state law, the federal courts, when necessary, decide both issues. Propper v. Clark, 337 U.S. 472, 490 (1949). The holdings of Swift and Propper, read together, suggest that a federal court should not abstain under Pullman from interpreting a state law that might be preempted by a federal law, because preemption problems are resolved through a non-constitutional

process of statutory construction. See 17 C. Wright, A. Miller & E. Cooper, Federal Practice and Procedure § 4242 at 454-55 (1978) (Pullman abstention inappropriate in a Supremacy Clause case); cf. 1A J. Moore, Federal Practice § 0.203[2] at 2141 (1985) (where clear conflict between federal and state statutes, no abstention appropriate).

Because USAA had pled other constitutional violations in its complaint, the district court declined to consider whether its preemption argument, taken alone justified preemption. USAA's preemption claim was the sole basis for its motion for summary judgment, however, and is easily separable from its other claims should USAA choose to purse them. Accordingly, we hold that preemption claims under the Supremacy Clause are not substantial federal constitutional issues for which Pullman

abstention might be appropriate.[4] Thus, the district court erred in deciding that the preemption claim also afforded a basis for abstention on Pullman grounds.

IV.

Under Burford, abstention is appropriate "where there have been presented difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar." Colorado River 424 U.S. at 814.

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[4]We note that a panel of this court has very recently held on other grounds that preemption questions are often not suitable for abstention under the doctrines announced in Burford and Younger. Kentucky West Virginia Gas co. v. Pennsylvania Public Utility Co., No. 85-5779 (3d Cir. June 2, 1986), slip op. at 10-11, 13-14.

If the exercise of federal review would be disruptive of state efforts to establish a coherent policy, and the policy concerns complicated local matters, abstention may be justified. Id. Generally, Burford abstention is justified where a complex regulatory scheme is administered by a specialized state tribunal having exclusive jurisdiction. See, Allegheny Airlines, Inc. v. Pennsylvania Public Utility Commission, 465 F.2d 237, 241-45 (3d Cir. 1972), cert. denied, 410 U.S. 943 (1973); see generally, 1A J. Moore, supra §0.203[2] at 2140-41 (collecting cases).

The district court in the present case found that Burford abstention was appropriate because the McCarran-Ferguson Act gave the states

exclusive control over the regulation of insurance, 15 U.S.C. § 1012 (1982), and because section 641 is part of a complex regulatory scheme governing insurance. It cited Levy v. Lewis, 635 F.2d 960 (2d Cir. 1980), which held that abstention was proper to allow a state regulatory body to settle claims against a liquidating insurer. The Levy court found it "highly significant that the state scheme has been adopted pursuant to congressional authorization" under McCarran-Ferguson, 635 F.2d at 963.

The Supreme Court has established a three-part test for determining whether state regulation is part of the business of insurance, 15 U.S.C. § 1012 (a) & (b), reserved to the states by McCarran-Ferguson:

> [F]irst, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry.

Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119, 129 (1982). "None of these criteria is necessarily determinative in itself." Id. The state regulations implicated in Levy concerned both the future coverage of policyholders and their relationship with a defunct insurer, and so were authorized under McCarran-Ferguson. The purpose of section 641, as stated in its part (c), is to prevent competition between insurers and Pennsylvania financial institutions. Unlike the regulations in Levy, the section is not concerned with

transferring or spreading the policyholder's risk; affiliation between insurers and banks has no integral connection to the relationship between the insured and insurer; and banks are not entities within the insurance industry. Regulations such as section 641 have no part in the business of insurance under McCarran-Ferguson.

The district court also thought Burford abstention was appropriate because section 641 is part of an "extensive and complicated . . . state regulatory scheme." The interpretation of section 641 in this case does not require consideration of any other Pennsylvania statute and the relevant facts are simple and undisputed; no complicated regulatory scheme is involved. The insurance department has not suggested any peculiar local conditions or special expertise required to interpret

the statute. The state proceeding merely involves reading and construing a statute, a task for which courts are best equipped, and not administrative factual determinations, such as are involved in the setting of a proper utility rate. The district court erred in applying Burford to this case.

V.

Under Younger, "interests of comity and federalism counsel federal courts to abstain from jurisdiction whenever federal claims have been or could be presented in ongoing state judicial proceedings that concern important state interests." Hawaii Housing, 467 U.S. at 237-38 (emphasis added). Younger abstention is required only when the state court proceedings are initiated prior to any proceedings

on the substance of the merits in federal court. Id. at 238. USAA argues that Younger abstention was inappropriate here because state proceedings did not commence until sometime after the federal suit was filed, and because these proceedings were administrative and could not address constitutional arguments.

The commencement of administrative proceedings after the federal suit was filed, even with the intention of removing federal jurisdiction by abstention, does not preclude the application of Younger. So long as "the federal litigation was in an embryonic stage and no contested matter had been decided," the district court may abstain under Younger. Doran v. Salem Inn, Inc., 422 U.S. 922, 929 (1975). In the present case, the district court had taken no

action on the substance of USAA's claim when administrative proceedings commenced.

This court has held that "where federal intervention into state administrative proceedings would be substantial and disruptive, and where the proceedings are adequate to vindicate federal claims and reflect strong and compelling state interests, the district court, pursuant to Younger, should abstain." Williams v. Red Bank Board of Education, 662 F.2d 1008, 1017 (3d Cir. 1981) (emphasis added). The Supreme Court, however, held in Hawaii Housing that administrative proceedings that are not part of, and are not themselves, judicial proceedings, do not trigger Younger abstention. 467 U.S. 238. In Hawaii Housing an administrative arbitration proceeding, by statute, was separate from any subsequent judicial

condemnation proceeding. In the present case, where an administrative decision to revoke USAA's insurance license could be appealed through the Pennsylvania courts, it is more difficult to determine whether the administrative proceeding is part of the state's judicial process.

USAA's federal claims are of constitutional dimension. As this court stated in Red Bank, administrative proceedings suffice for Younger purposes only when they "are adequate to vindicate federal claims." The Supreme Court has held that administrative proceedings that are forbidden by state law from considering federal constitutional claims will not invoke Younger because there is no "adequate opportunity in the state proceedings to raise constitutional challenges." Middlesex Ethics Comm. v. Garden State Bar Ass'n, 457 U.S.

423, 432 (1982). We believe a state administrative proceeding is part of its judicial process, for Younger purposes, only if it provides an adequate opportunity to raise constitutional challenges.

It appears to be settled law in Pennsylvania that an administrative agency may not determine the constitutionality of the statutes it applies. Borough of Green Tree v. Board, 328 A.2d 819, 825 (Pa. 1974); Delaware Valley v. Commissioner, 389 A.2d 234, 237 (Pa. Comm. Ct. 1978). The insurance department in its internal documents has acknowledged this limitation. Because the insurance department in its administrative proceedings cannot consider USAA's constitutional arguments, its administrative proceedings are not part

of Pennsylvania's judicial process and the district court erred in abstaining under Younger.

VI.

We conclude that the district court erred in abstaining from considering USAA's preemption claim and dismissing its suit. The order of dismissal will be reversed and the case remanded to the district court for proceedings consistent with this opinion.

BECKER, Circuit Judge, concurring.

In [sic] concur in the judgment and in all but Part III.B of the majority's opinion. I write separately to explain my disagreement with one ground for the majority's holding that Pullman abstention is improper in this case. The majority states that the balance of

the interests disfavors abstention because the potential damage to United Services Automobile Association's ("USAA") business during state administrative and court proceedings outweighs the state interests in abstention. I disagree, however, and believe that such a holding may have dangerously broad implications.

There are certainly cases in which the burdens imposed upon a plaintiff by abstention outweigh the interests served by application of the Pullman rule and in which the balance of interests therefore counsels against abstention. However, I do not believe that this is such a case. The state administrative and judicial proceedings that USAA would face are no more cumbersome than the state procedures available to any state litigant. The fact that

USAA would have to receive an administrative ruling before it could present its case to a state court does not render its situation significantly more harmful than it if [sic] could proceed directly to federal court.[1] By permitting USAA to prevail on this argument, the majority creates a precedent that could allow virtually any litigant faced with relatively complex state litigation to avoid the application of the Pullman abstention doctrine.

USAA has convinced the majority that ongoing license revocation litigation would drastically damage its reputation and thus impair its marketing

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[1]This is especially true because the administrative hearing is over and the administrative decision will apparently be announced soon.

of insurance. I am not convinced, however, that the harm that such litigation would impose upon USAA is significantly different from or greater than the harm that important ongoing litigation imposes upon any litigant. For example, if a company were threatened with a large fine or penalty as the result of a state proceeding, the litigation might affect the value of its stock. Yet I do not believe that this predictable side-effect of litigation would justify a denial of Pullman abstention, if abstention were otherwise proper. In Bellotti v. Baird, 428 U.S. 132 (1976), the continuing existence of a statute that governed the type of consent required before an abortion could be performed on a woman under the age of eighteen imposed a substantial burden on individuals

to whom it applied. Although the Court acknowledged that "[e]ach day the statute is in effect, irretrievable events, with substantial personal consequences, occur," 428 U.S. at 151, it nevertheless held that abstention was proper. I do not believe that the type of harm that abstention would inflict upon USAA in this case is any greater than the type of harm caused to young women during that state litigation ordered in Bellotti v. Baird.

It is significant that, as the majority has pointed out, the insurance department has proposed ways of mitigating the harm that state litigation would impose upon USAA. It "has indicated a willingness to expedite consideration of USAA's claims in state procedures, and to agree to a stay of

execution in the event of an administrative decision adverse to USAA until judicial proceedings were completed." Maj. Op. at 11. Such expedition reduces the burden that resort to the state system creates for USAA. Cf. Bellotti v. Baird, supra. 428 U.S. at 150-51 (procedure for certifying issues directly to the state supreme court reduces relative burden of abstention, so that abstention is appropriate even in case in which the "importance of speed in resolution . . . is manifest"). The proposed stay of execution of a license revocation order also distinguishes this case from Pike v. Bruce Church, Inc., 397 U.S. 137 (1970), cited by the majority, in which the plaintiffs were subject to a state enforcement order which would impair their existing business activity.

Because I believe that the harm threatened to USAA is not significantly greater than the harm that state litigation would inflict upon any litigant, I believe that the majority's assessment of the balance of the interests in this case creates an exception that could swallow the abstention rule. Indeed, almost any litigant opposing Pullman abstention can make out a case as strong as USAA's. I think that the balance of the interests approach as a basis for avoiding Pullman abstention should be reserved for extreme cases, such as Pike v. Bruce Church, Inc., Supra, 397 U.S. at 139, in which an emergency situation was presented because the company faced an imminent loss of its cantaloupe crop

as a result of a state enforcement order, while only "a narrow and specific application" of a state statute was challenged as unconstitutional).[2]

I do, however, agree with the majority's other ground for holding that this is not a proper case for Pullman abstention: Pullman abstention should not be employed to avoid a ruling on a claim of federal preemption because such

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[2]Not only do I find that the harm that abstention would impose upon USAA in this case is not unusually great, but I also find that the countervailing state interest in interpreting its regulation is not unusually small. Unlike the situation in McKnight v. Southeastern Pennsylvania Transportation Authority, 583 F.2d 1229, 1241 (3d Cir. 1978), in which resolution of the constitutional issue before definitive state interpretation of a statute "would not upset sensitive state programs," federal intervention into the interpretation of Pennsylvania insurance regulations would be quite intrusive.

a claim does not call for substantial federal constitutional adjudication. I would base the holding on that ground alone.

A True Copy:

Teste:

Clerk of the United States Court of for the Third Circuit

EXCERPTS OF PENNSYLVANIA'S STATUTES GOVERNING JUDICIAL REVIEW OF COMMONWEALTH AGENCY ACTION

2 Pa.Cons.Stat.Ann.

Section 703. Scope of review

(a) General rule.--A party who proceeded before a Commonwealth agency under the terms of a particular statute shall not be precluded from questioning the validity of the statute in the appeal, but such party may not raise upon appeal any other question not raised before the agency (notwithstanding the fact that the agency may not be competent to resolve such question) unless allowed by the court upon due cause shown.

* * * *

Section 704. Disposition of appeal

The court shall hear the appeal without a jury on the record certified by the Commonwealth agency. After hearing, the court shall affirm the adjudication unless it shall find that the adjudication is in violation of the constitutional rights of the appellant, or is not in accordance with law, or that the provisions of Subchapter A of Chapter 5 (relating to practice and procedure

of Commonwealth agencies) have been violated in the proceedings before the agency, or that any finding of fact made by the agency and necessary to support its adjudication is not supported by substantial evidence. If the adjudication is not affirmed, the court may enter any order authorized by 42 Pa.C.S. §706 (relating to disposition of appeals).

RULE 1781, PA.RULE OF APPELLATE PROCEDURE

Stay Pending Action of Petition for Review

(a) Application to government unit. Application for a stay or supersedeas of an order or other determination of any government unit pending review in an appellate court on petition for review shall ordinarily be made in the first instance to the government unit.

(b) Contents of Application for stay or supersedeas. An application for stay or supersedeas of an order or other determination of a government unit, or for an order granting an injunction pending review, or for relief in the nature of preemptory mandamus, may be made

to the appellate court or to a judge thereof, but the application shall show that application to the government unit for the relief sought is not practicable, or that application has been made to the government unit and denied, with the reasons given by it for the denial, or that the action of the government unit did not afford the relief which the applicant had requested. The application shall also show the reasons for the relief requested and the facts relied upon, and if the facts are subject to dispute the application shall be supported by sworn or verified statements or copies thereof. With the application shall be filed such parts, if any, of the record as are relevant to the relief sought.

(c) Notice and action by court. Upon such notice to the government unit as is required by Rule 123 (application for relief) the appellate court, or a judge thereof, may grant an order of stay or supersedeas, including the grant of an injunction pending review or relief in the nature of preemptory mandamus, upon such terms and conditions, including the filing of security, as the court or the judge thereof may

prescribe. Where a statute requires that security be filed as a condition to obtaining a supersedeas, the court shall require adequate security.

EXCERPTS OF PENNSYLVANIA JUDICIAL CODE

42 Pa.Cons.Stat.Ann.

Section 724. Allowance of appeals from Superior and Commonwealth Courts

(a) General rule.--Except as provided by section 9781(f) (relating to limitation on additional appellate review), final orders of the Superior Court and final orders of the Commonwealth Court not appealable under section 723 (relating to appeals from Commonwealth Court) may be reviewed by the Supreme Court upon allowance of appeal by any two justices of the Supreme Court upon petition of any party to the matter. If the petition shall be granted, the Supreme Court shall have jurisdiction to review the order in the manner provided by section 5105(d)(1) (relating to scope of appeal).

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Section 763. Direct appeals from government agencies

(a) General rule.--Except as provided in subsection (c), the Commonwealth Court shall have exclusive jurisdiction of appeals from final orders of government agencies in the following cases:

(1) All appeals from Commonwealth agencies under Subchapter A of Chapter 7 of Title 2 (relating to judicial review of Commonwealth agency action) or otherwise and including appeals from the Environmental Hearing Board, the Pennsylvania Public Utility Commission, the Unemployment Compensation Board of Review and from any other Commonwealth agency having Statewide jurisdiction.

(2) All appeals jurisdiction of which is vested in the Commonwealth Court by any statute hereafter enacted.